BEFORE THE DEPARTMENT OF REVENUE
OF THE STATE OF MONTANA

In the matter of the adoption of New Rules I through III and the amendment of ARM 42.12.101, 42.12.106, 42.12.111, 42.12.126, 42.12.137, 42.12.143, and 42.12.315 regarding liquor licenses	))))))	NOTICE OF ADOPTION AND AMENDMENT

TO: All Concerned Persons

1. On December 26, 2013, the Department of Revenue published MAR Notice Number 42-2-904 pertaining to the public hearing on the proposed adoption and amendment of the above-stated rules at page 2406 of the 2013 Montana Administrative Register, Issue Number 24.

2. On January 27, 2014, a public hearing was held to consider the proposed adoption and amendments. Neil Peterson of the Gaming Industry Association (GIA), John Iverson of the Montana Tavern Association (MTA), Janet Prescott, Secretary of the MTA and an all-beverages liquor license owner, and Joel Silverman, all appeared and testified at the hearing. The department also received written comments from Ronda Wiggers of the Montana Coin Machine Operators Association (MCMOA).

3. The department has adopted New Rule I (42.12.105), New Rule II (42.12.317), and New Rule III (42.12.316), and amended ARM 42.12.111, 42.12.126, 42.12.137, and 42.12.315, as proposed.

4. Based upon the comments received and after further review, the department has amended the following rules as proposed, but with the following changes from the original proposal, new matter underlined, deleted matter interlined:

42.12.101 APPLICATION FOR LICENSE (1) through (4) remain as proposed.

(5) ~~Following approval of an application, the~~ The licensee remains bound by all requirements in statute and rule that apply ~~to an applicant~~ at the time ~~of~~ an application for license or an application for renewal is approved. A licensee's failure to remain in compliance with a statute or rule shall constitute a violation of that statute or rule and may subject the licensee to ~~penalties~~ administrative action.

(6) through (14) remain as proposed.

42.12.106 DEFINITIONS The following definitions apply to this chapter:

(1) "Affiliation" means relationships ~~including, but not limited to, those wherein a party directly or indirectly~~ wherein:

(a) an entity owns or controls another ~~party, parties~~ entity;

(b) entities are under common ownership or control~~, and one party is a~~

~~subordinate or employee of another party~~; or

(c) an individual has decision-making authority or influence over business decisions for another entity.

(2) through (12) remain as proposed.

(13) "Family relationship" means a spouse, dependent children, or dependent parents.

(13) through (32) remain as proposed, but are renumbered (14) through (33).

42.12.143 RESTRICTION ON INTEREST IN OTHER LICENSES (1) and (2) remain as proposed.

(3) A Montana retail alcoholic beverages licensee may not:

(a) remains as proposed.

(b) individually or through the person's immediate family, receive financing from or have any affiliation to:

(i) an alcoholic beverage manufacturer~~;~~

~~(ii) an~~ or importer of alcoholic beverages; or

(iii) remains the same but is renumbered (ii).

(4) through (6) remain as proposed.

5. The department thoroughly considered the comments and testimony received. A summary of the comments and the department's responses are as follows:

COMMENT NO. 1: Mr. Peterson commented that ARM 42.12.101(5), which provides, in part, that "a licensee's failure to remain in compliance with a statute or rule shall constitute a violation of that statute or rule and may subject the licensee to penalties" appears to be at odds with existing ARM 42.12.122(5), which states that a currently licensed premises that does not meet the suitability standards are required to meet the standards upon seeking department approval of alterations. Essentially, there is a grandfather clause in there for suitability of premises should the requirements change.

Mr. Peterson asked the department to consider amending the second sentence in that section to reference the grandfather clause in ARM 42.12.122(5) to make it clear that a licensee need not immediately comply with statute or rule changes related to their licensed premises until they seek to alter their licensed premises.

RESPONSE NO. 1: The department has made slight amendments to the proposed rule to reflect that the continued obligation is tied to the date the original application is approved and the date when each subsequent renewal is approved. The department also amended the rule to clarify that violating a continuing obligation could subject the licensee to administrative action rather than penalties. This was done to ensure that licensees understood that administrative action encompassed more than just monetary penalties. These amendments clarify the rule language to carry out its original intention. While the department appreciates Mr. Peterson's comments, it does not find it necessary to amend the rule further because the rule as proposed does not conflict with ARM 42.12.122(5).

COMMENT NO. 2: The department received the following comments regarding the proposed definition of the term "affiliation" in ARM 42.12.106.

Mr. Peterson stated that the GIA believes the definition is overly broad and will create some unintended consequences related to the ownership of various alcohol beverage licenses. Specifically, the last part of the definition which states "one party is a subordinate or employee of another party" may constitute an affiliation for the purposes of Senate Bill (SB) 120, but the GIA believes it also impacts other areas in current statute and rule and may cause some serious problems for members.

He provided the example of members who currently own a license and at the same time are employees of businesses whose owners also own a license. Suppose an employee's father owns a license in a small quota area and he or she has a small minority interest in that license but doesn't even live in that town. As the GIA reads the proposed new definition, that employee's employer may be barred from buying a license in that small quota area because of that relationship or affiliation.

Mr. Peterson provided another scenario, that doesn't deal directly with SB 120, where an owner of a video gaming machine manufacturer also has an ownership interest in a small brewery. Would his employees be prohibited from owning a retail license due to the employee/employer relationship? This doesn't seem right and is a substantial change from current statute and rules in this area that deal with immediate or dependent family members owning licenses in different tiers of the three-tier system.

He stated that the GIA doesn't believe that was the department's intent, and suggests striking the proposed language in the definition dealing with "one party is a subordinate or employee of another party." SB 120 does not use the term affiliation, nor is the term used in the proposed changes to ARM 42.12.143. There is no reference to affiliation. The term affiliation is currently used in statute in reference to ownership of a license in separate tiers of the state's three-tier system of regulating the sale of alcohol in 16-4-401, MCA.

Mr. Iverson commented that some MTA members feel the definition provided for affiliation creates confusion and that they don't understand what it does or does not mean. He commented that while his members didn't make suggestions for language changes, they did ask that the language be clarified.

Mr. Silverman expressed concern about the proposed definition and asked how far down the road this will go. When talking about control, directly or indirectly, does an affiliation lead also to independent contractors? Does it mean that a bar owner's child, as an immediate family member, cannot work for one of the other two tiers? Could there suddenly be a violation issued if it is determined that a bar owner's dependent child, who's working for a distributor, has an affiliation through other tiers? And how would that violation work? It's not laid out in the structure of ARM 42.13.101, and may require new rules as to how the violations would be administered. He stated that this goes beyond just the employee status and has never really been applied in the past.

Also, with regard to the definition, Mr. Silverman asked about management agreements. Would affiliation rise to a subordinate level and then could someone

not work as a manager while also owning another license in a different tier? With regard to those who are already grandfathered in, would they be in violation because of this new definition? Would they have to forgo their license or receive a violation on renewal?

Ms. Prescott stated that affiliation, according to the dictionary or Google, has many definitions, including but not limited to membership interaction, togetherness, club association, clubs, religion, and political affiliation. She commented that she believes the language in the rule needs to be clarified in depth. While the language might be understood currently, five years down the road it could mean that two people who are Shriners or Rotarians together could not own a license because they have a joint or close affiliation that might be construed as inappropriate.

Ms. Wiggers commented that the proposed definition is too broad to be practical in Montana. She stated that while the MCMOA understands the intent to maintain the integrity of the three-tier system, this appears to unintentionally catch more than that.

She commented that many of her route operators are also invested in multiple other businesses in Montana. Some have investments in real estate, hotels, insurance companies, and the like. In many cases, they also own a liquor license.

Would this prohibit the spouse of one of their insurance company employees from owning a brewery license? The current language appears to unnecessarily create this problem. If a route operator owns the insurance agency and the liquor license both, their insurance employee would be "employed" by someone owning this license. Then, through the person's "immediate family" clause, their spouse would not be allowed to own a manufacturer license.

By including the "employee," "indirectly owns," and "common ownership" language in the definition of affiliated, and then applying that to the language in ARM 42.12.101, "individually, or through the person's immediate family, receive financial support from or have any affiliation to," the department has created a complicated situation where businesses not involved in liquor could be eliminated from owning a liquor license.

Ms. Wiggers provided the example of someone who owned a vending business and also owned a beer distributorship at the same time. Several employees of the vending business either owned liquor licenses or were married to someone who owned one. Under this proposed rule, it appears that situation would not be legal even though the vending business was not connected to the distributorship beyond the vendor owner's investment. She stated that they are confident that this was not the department's intent and would like to see the department adopt a rule more concise in application.

RESPONSE NO. 2: The department appreciates these comments from the industry and has further amended the definition of affiliation in ARM 42.12.106 in response. "Affiliation" has been amended to prohibit licensees and their immediate family from having decision-making authority or influence in business decisions in another tier.

COMMENT NO. 3: The department received the following comments regarding the proposed definition of the term "stand-alone beer and/or table wine business" in

ARM 42.12.106.

Mr. Peterson stated that the GIA feels the proposed definition is unnecessary and introduces new requirements not envisioned in House Bill (HB) 524. The purpose of HB 524 was to eliminate the requirement that an off-premises beer and wine license be affiliated with either a grocery store or pharmacy. That change would facilitate the business model of specialty wine and beer stores.

The proposed definition states that a stand-alone beer and/or table wine business derive at least 95 percent of its business from the sale of beer or wine, allowing for 5 percent of revenues from the sale of other types of products. Mr. Peterson commented that the GIA thinks that requirement is administratively unworkable for both the department and the licensee, and asked if a licensee, during the last week of the year, is supposed to refuse to sell certain items to the public for fear they would violate the 95 percent requirement. This is not practical for licensees and would further confuse the public concerning Montana's scheme to regulate the sale of alcoholic beverages.

If the department feels a definition is needed, Mr. Peterson submits that a better approach would be to amend the rule to require business revenues to be predominantly from the sale of beer and/or table wine, with any other revenue from the business being derived from items commonly found in a grocery store, convenience store, or pharmacy.

Ms. Wiggers commented that the definition does not appear to reflect the intent of the legislature to simply eliminate the need for a wine store to act as a grocery store. She stated her understanding was that the legislature was trying to eliminate the need for a wine store to carry five different types of food products just to comply; they were not intending to limit the wine store's ability to sell food or stemware if it so chooses. This rule seems to simply create another problem to take to the legislature. Why create a new license? Ms. Wiggins instead suggests removing the rule referring to the grocery requirements for a beer/wine off-premises license.

RESPONSE NO. 3: The department appreciates these comments but has determined that no further amendments will be made to the definition. Prior to proposing this rule, the department consulted with the sponsor of HB 524. The intent of HB 524 was to allow a licensee to sell beer and/or table wine without having to operate as a grocery store or drugstore licensed as a pharmacy. However, if the licensee were to operate in conjunction with another business, that business must be a grocery store or drugstore licensed as a pharmacy. The sponsor indicated that requiring the licensee to derive at least 95 percent of its annual gross sales from beer and/or table wine maintained the intent of the legislation.

COMMENT NO. 4: The department received the following comments regarding the proposed language in ARM 42.12.143 regarding a business or family relationship.

Mr. Iverson stated that the meaning of the family relationship is unclear and asked that when the department uses the term family relationship or immediate family, it clarify exactly what is or is not a family relationship and what is or is not immediate family. The rules are there to clarify the law and should be crystal clear regarding the

term immediate family member.

Mr. Silverman reiterated Mr. Iverson's point with regard to family relationship not being defined in the rules or statutes. He commented that it would be nice, from a clarity standpoint, if the rule just referred back or used the phrase immediate family, so that everyone would be on the same page and understand the application of the term.

Mr. Silverman also referred to the department's general definitions rule, ARM 42.2.304, and commended the department for previously revising the lead-in language of that rule to refer to definitions as found in statute unless a particular chapter provides otherwise. "Immediate family member," as defined in ARM 42.2.304(25), goes to a tax administrative rule instead of a liquor rule. "Immediate family" is defined in Title 16, MCA.

Ms. Prescott stated that she and some other all-beverage licensees she has talked to have a number of questions and would like clarification regarding, but maybe not be limited to, ARM 42.13.143. Specifically, in (2)(b), the definition of family relationship and what exactly that entails and how far along the family tree this would pertain. With regard to sharing profits and liabilities, Ms. Prescott commented that she believes the shared profits and liabilities is pretty broad, because the rule itself was totally to control the total number of all-beverage licenses in the specific quota area. But with the shared profits and liabilities clause, the question would be, what does that pertain to?

For instance, if one licensed member used her profits to purchase dinner for another licensed member, would the recipient of that dinner be considered to be sharing in the profits of the purchaser's license? While this example is a stretch, they are concerned about unintended consequences and what the association of profits and liabilities might be in a ruling, such as a non-business property, from a vacation rental in Hawaii to anything where there might be unassociated family members joined in a totally separate entity. She asked for clarification on that.

RESPONSE NO. 4: As a preliminary matter, the department notes its amendment to the format in ARM 42.12.143(3) for consistency with other sections of that rule. No substantive edits are made to that section.

The department appreciates the comments regarding the ownership limitation imposed by SB 120 on individuals who "through business or family relationship share in profits or liabilities of all-beverages licenses," which is reflected in ARM 42.12.143.

Many of the comments addressed concerns regarding the use of the term "family relationship" in 16-4-401(8), MCA. It is noted that elsewhere throughout that statute, the term "immediate family" is used. "Immediate family" is defined in 16-1-106(13), MCA, to encompass a spouse, dependent children, and dependent parents. The department believes that the reference in 16-4-401(8), MCA, to a "family relationship" was intended to use the statutory definition of "immediate family." Accordingly, the department has further amended ARM 42.12.106, to define "family relationship" based upon the statutory definition of immediate family.

The department has also reviewed the concern regarding what constitutes the sharing of profits and liabilities but declines to make any further amendments to the rule at this time. The language about sharing in the profits or liabilities is derived from statute and the department intends to keep this language consistent with the statute. Additionally, the department finds that this phrasing does not necessitate additional

definition. It does not find that purchasing dinner for another licensee constitutes the act of sharing in profits and liabilities.

COMMENT NO. 5: Ms. Prescott commented on the provision in ARM 42.12.315(4) that provides that applicants for sacramental wine licenses are not subject to fingerprint or background checks. She explained that they have been working, very specifically, to ensure that any time there is a liquor license, whether it is for beer, wine, or anything else, that every applicant is screened and duly vetted by the department equally. Ms. Prescott stated that with the issues that might happen in clergy, she doesn't believe they are necessarily above the law and that they should be vetted equally with others.

RESPONSE NO. 5: The department has reviewed this comment and determined that the removal or amendment of ARM 42.12.315(4) is unwarranted. Senate Bill 266, L. 2013, removed language allowing the department to request a Department of Justice background investigation on sacramental wine license applications. Thus, the department included new (4) to highlight a determination made by the Legislature; it was not making the determination itself.

6. An electronic copy of this notice is available on the department's web site, revenue.mt.gov. Select the Administrative Rules link under the Other Resources section located in the body of the homepage and open the Adoption Notices section within. The department strives to make the electronic copy of this notice conform to the official version of the notice, as printed in the Montana Administrative Register, but advises all concerned persons that in the event of a discrepancy between the official printed text of the notice and the electronic version of the notice, only the official printed text will be considered. While the department also strives to keep its web site accessible at all times, in some instances it may be temporarily unavailable due to system maintenance or technical problems.

/s/ Laurie Logan
LAURIE LOGAN
Rule Reviewer

/s/ Mike Kadas
MIKE KADAS
Director of Revenue

Certified to the Secretary of State on June 2, 2014